



BILL DRAFT 2007-RBz-33: Modify Estate Tax Law

BILL ANALYSIS

Committee:	Revenue Laws Study Committee	Date:	April 2, 2008
Introduced by:		Summary by:	Cindy Avrette
Version:	Bill Draft		Committee Staff

SUMMARY: *This bill draft would modify the formula for calculating North Carolina estate tax on estates that include property located in another state by excluding the value of that property from the estate tax payable to North Carolina. The bill would become effective when it becomes law and apply retroactively to the estates of decedents for which the statute of limitations for claiming a refund had not expired as of December 28, 2007.*

CURRENT LAW: For estates with property only in North Carolina, the North Carolina estate tax equals the amount of the credit for state estate tax allowed on the federal estate tax return, as the federal law provided in 2001. If an estate has property in more than one state, the federal credit amount must be prorated between North Carolina and the other states in which the estate has property. In 2002, the Estate Tax Section of the North Carolina Bar Association recommended a change in the calculation formula from a net value ratio to a gross value ratio. The recommended change also provided that when the estate of a North Carolina decedent included out-of-state property, the North Carolina estate tax would be calculated as the amount of the 2001 tax credit reduced by *the lesser of* the amount of estate tax paid to the other state or the amount of the 2001 tax credit times the value of the out-of-state property divided by the value of the gross estate.¹

In 2001, Congress phased out the state estate tax credit over four years by reducing it 25% in 2002, 50% in 2003, 75% in 2004, and by repealing it entirely in 2005.² In calculating the estate tax payable in North Carolina for an estate that includes property located in a state that does not impose an estate tax, the current formula provides that the North Carolina estate tax would be reduced by zero, because that is the lesser of the amount paid to the state that does not impose an estate tax. This calculation results in North Carolina's estate tax being imposed on property that is not located within its taxing jurisdiction.³

BILL ANALYSIS: This bill draft would modify the formula for calculating North Carolina estate tax on estates that include property located in another state by prorating the federal credit amount between North Carolina and the other states in which the estate has property; it would eliminate the 'lesser of' language that sometimes results in North Carolina's estate tax being imposed on property located in another state.

A case has been filed in Mecklenburg County, *Stowe v. Department of Revenue*, to recover North Carolina estate taxes imposed on property located in South Carolina. The plaintiffs argue in their

¹ This provision mirrored the Virginia law as it existed prior to July 1, 2007.

² The provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 made a number of changes to the estate tax rates and to the applicable exclusion amounts. The top marginal tax rates were gradually reduced and the exclusion amounts were gradually increased, with a full repeal of the estate tax for 2010. For 2007 through 2009, the top marginal tax rate is 45%; for 2007 and 2008, the applicable exclusion amount is \$2,000,000; for 2009, the applicable exclusion amount is \$3,500,000. The provisions for these changes are currently set to expire for estates of decedents dying on or after December 31, 2010. Therefore, in 2011, the exclusion amount goes back to \$1,000,000, the top marginal rate returns to 55%, and the state estate tax credit is reinstated.

³ Virginia repealed its estate tax in 2006. South Carolina, Georgia, and Tennessee do not require the payment of an estate tax for estates on which the federal estate tax law does not allow a credit for state estate tax (2005-through 2010).

complaint that the formula for calculating North Carolina estate tax due when property is located in more than one state is unconstitutional because it provides less than a full reduction of the tax attributable to the out-of-state property when the other state does not impose an estate tax, or imposes an estate tax less than the prorated federal credit amount. The plaintiffs filed the complaint on December 27, 2007.

The bill draft provides that the change proposed in the bill would become effective when it becomes law and would apply retroactively to the estates of decedents for which the statute of limitations for claiming a refund had not expired on December 27, 2007. A personal representative of an estate for which the statute of limitations had not expired may file a claim for refund under G.S. 105-241.6.

G.S. 105-241.6 provides that the general statute of limitations for obtaining a refund of an overpayment of tax is the later of the following:

- Three years after the due date of the return. – A North Carolina estate tax return is due on the date a federal estate tax return is due. A federal estate tax return is due nine months from the date of death. An extension of time to file a federal estate tax return is an automatic extension of the time to file a State tax return.
- Two years after payment of the tax.